A trader CHECKLIST

Do you have what it takes to make a living in the markets? One short-term trader offers some thoughts on the typical characteristics and skills of successful traders.

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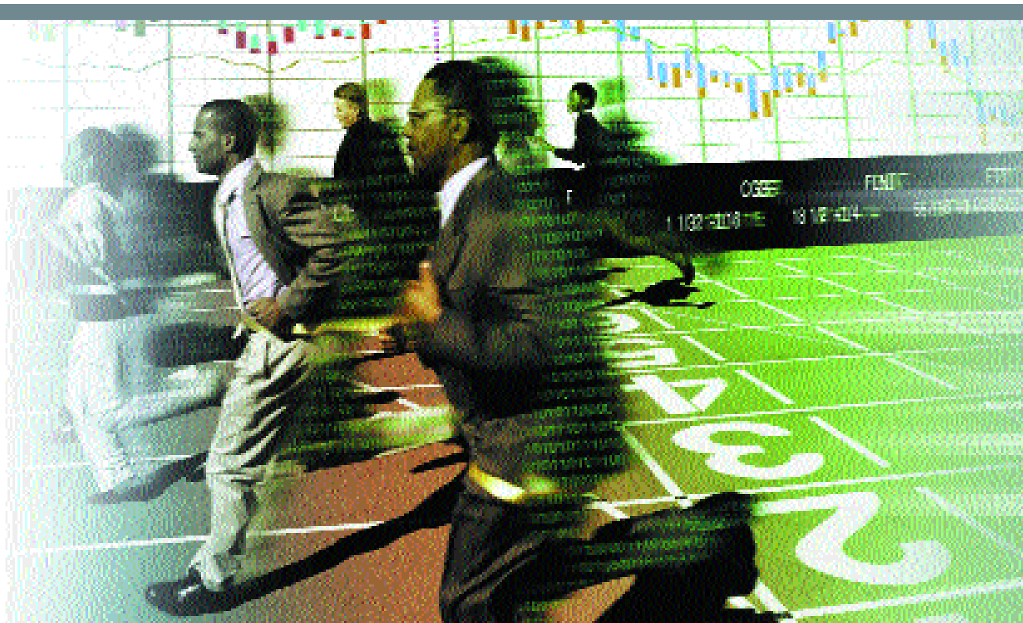


There are two questions almost all new traders ask: "What does it take to trade?" and "How long does it take to learn to trade?"

These are difficult questions, because the answers will vary from trader to trader. Although some would-be traders have an innate understanding of the markets and what it takes to be profitable, others are less intuitive and will require many years to become successful — if they can survive that long. Still others fall in the middle: They have an average learning capacity, and might become successful after a couple of years or so.

However, there are several factors — ranging from your lifestyle to your psychological makeup — you can analyze to help determine if you are suited to making a living in the markets. In no particular order, they are:

- Aptitude and psychology,
- Attitude and confidence,
- Focus and discipline,
- Lifestyle,
- Patience and judgment,
- Trading capital,
- Perseverance, and
- Risk management.

As you read through these topics, give yourself on honest appraisal about how closely you match the characteristics of successful traders and whether you have the necessary financial and time resources.

This is not intended to be a test that concretely determines your trading ability. It is simply a self-evaluation tool for prospective traders that can reveal areas needing improvement before you begin risking money. Also, it is a good idea to occasionally review these subjects even after you become a better trader to see how much you've progressed and what you've learned.

Aptitude and psychology

This consists of all your mental faculties — e.g., memory, problem solving, quick reflexes, and "on-your-feet" decision-making skills — and the ability to integrate these talents. Although a person's actual IQ may or may not have anything to do with his or her trading ability, having a high one doesn't hurt. Analytical, independent thinkers comfortable with mathematical concepts and probabilities, and who enjoy challenges often excel at trading.

Because of the challenge trading poses, your desire to succeed must be exceptionally high. Trading often attracts many people who were quite successful in another field — after all, people do not accrue the capital necessary to trade by failing. And it can be true the skills you developed that led to your prosperity in your previous field will be an asset in your trading career.

The catch is that successful people often have large egos. They believe success in their prior careers will naturally carry over into trading. However, trading requires more discipline than almost any other profession. Traders go into the wealth war every day and fight money battles all day long.

Do you have the mindset to sustain the bruises to your ego, not to mention your pocketbook, when the market turns on you? Can you stay in there fighting, day in and day out, to get the job done? If you have humility, know the financial markets are smarter than you, and can live with having your ego crushed quite frequently, you have the proper psychological makeup for trading.

Attitude and confidence

If people read *The Power of Positive Thinking* by Norman Vincent Peale, they would probably approach the markets with a much better attitude. However, after traders experience some losses, their attitudes may change from positive to negative.

It is important to understand and manage these mood swings. When they occur, you should momentarily step aside from trading or get an "attitude adjustment." Be aware that you will lose money, especially in the early part of your trading career. Think of your losses as the tuition you pay for the education the market gives you.

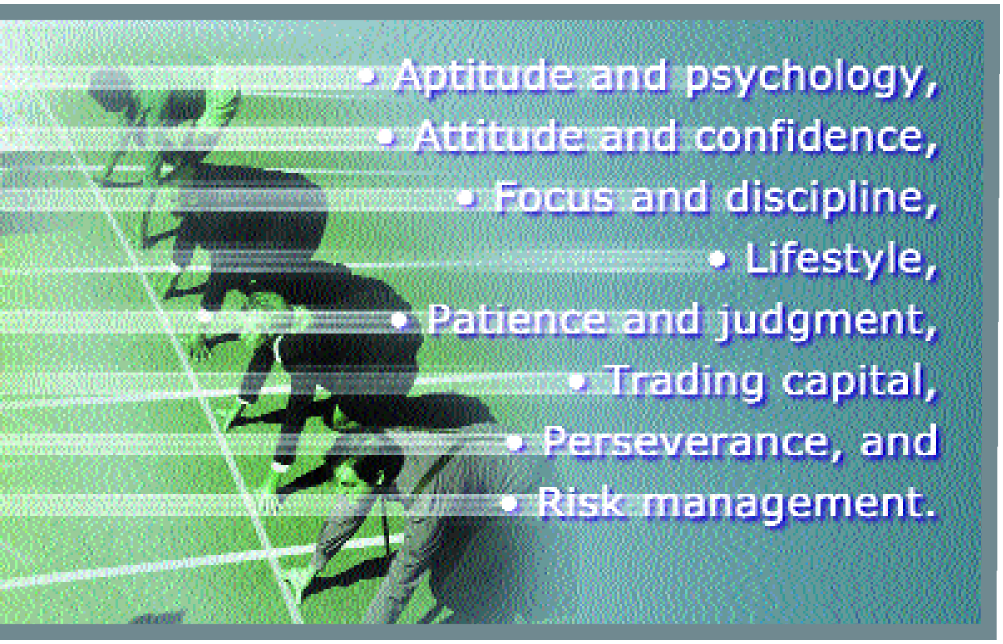
Self-confidence counts for a lot in trading, just as it does in every walk of life. Without confidence, you will not succeed; like attitude, your confidence will change when you suffer a few losses. Traders who wake up every morning confident they will make money are approaching the markets with the proper mindset.

Focus and discipline

Trading requires concentration. It will be difficult to trade effectively if your children continually bother you while you are working. Likewise, avoid reading your e-mail and turn the phone ringer off during market hours. Discourage your friends and family from contacting you while you are trading. If possible, handle important, non-trading matters during the market doldrums and then get back to work.

Ideally (although this is not possible for everybody) traders should take two 15-minute breaks during market hours, and then a substantial break between the end of the day's trading and the start of research for the next day.

Trading requires a great deal of study. The most successful traders research and prepare for the next day's trading with great precision and attention. Every day — including weekends — you must scan chart patterns and study the market. You must develop a detailed trading plan that maps out your actions for when things go wrong as well as for when they are going your way, and you must be able to stick to this plan in the face of adversity.



Lifestyle

Everybody wants to make money trading, but not everybody is willing to pay the price to accomplish that goal. It is difficult for a part-time trader to be successful. It is rare that someone can take time off from his or her other interests or jobs and learn to trade effectively. However, some people can learn enough to put on a few low-risk trades per week — accompanied by appropriate stops — and pursue their other interests. In most cases, though, being a successful trader requires anywhere between 50 and 70 hours of work per week. So, to learn the business, you must like it.

Successful traders jump into the profession with both feet and immerse themselves in the subject matter. If you like to stay out partying all night, this profession is not for you. You need a stable life to learn this vocation, and sleep is especially essential.

If you think the trading lifestyle is too demanding — and it can be particularly taxing if you live on the West Coast, where the markets open at 6:30 a.m. — you have two choices: Learn how to live with it, or find something else to do. If you have little children who are in need of constant attention, perhaps you should wait until they are older before you take on this new vocation.

Be realistic about the impact your spouse, parents or other influential people in your life can have on your new profession. If those close to you have a negative outlook on your trading, it may cut into your enthusiasm and confidence and adversely affect your performance. Know whether it's practical for you to engage in trading when doing so may strain key relationships in your life.

Also, be aware of the fact that you will lose money, especially in the early going. Think of your losses as tuition for the

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education the market gives you.

Patience and judgment

The perfect trader would be someone who was a video game enthusiast as a child, a skateboarder as an adolescent and a surfer as a young adult. Such as person would likely have the ability to quickly identify significant obstacles looming on the horizon and react before getting into serious trouble. Similarly, they would learn not to overreact to minor obstacles and setbacks. In other words, they balance quick reflexes with patience and judgment.

Judgment makes all the difference in short-term trading. Short-term traders need to wait patiently for confirmed setups and then execute their trading plans without hesitation. Waiting until a trade setup is complete requires a great deal of patience. On the other hand, there is only one "right moment" for each trade, and knowing when to act demands critical judgment.

Trading capital

What do you want to accomplish as a trader? Do you want to double your trading account? Make enough money to live on? Earn some extra cash on the side?

Whatever your trading goals are, it is imperative to first consider the size of your trading account and how it relates to your personal wealth. The SEC requires pattern day traders (those who make four or more day trades in a five-day period) to maintain $25,000 balances in their accounts.

All traders, regardless of how long they have been trading or what prior success they have had, should keep at least $30,000-$50,000 in their accounts at all times. How much money each trader needs can be determined more precisely by testing a trading strategy before trading it. Some trading ideas risk more than others, and will require a higher level of capitalization. If you don't have enough money to trade your strategy conservatively, you won't be able to stay in the market.

Also, the funds in your trading account must be money that is not needed for essential living expenses — the mortgage, children's education. Because new traders almost always lose money before they make it, you cannot afford to rely on your trading account to pay the bills.

Having adequate capitalization will enable you to "pay" yourself (i.e., take money out and put it in a personal account while your trading account maintains or even increases its balance) on a weekly or monthly basis.

Perseverance

Good traders need drive, determination and persistence.

Trading is a potentially rewarding, but decidedly difficult road to travel. Jumping blindly into trading is a direct path to the poorhouse. Just ask any of the tens of thousands of temporarily wealthy individuals who lost considerable amounts of money in 2000 and 2001. Even more traders take a stab at trading and lose just enough money to scare them out of the market — before they gain the experience and knowledge that leads to sustained profitability.

Of every 20 traders who enter the market, it is likely that only one will still be trading a year from now. Unless you commit to trading as a career and lifestyle, you will almost certainly fail.

Risk management

Another phrase for risk management is "knowing when and where to stop." Virtually every trading book ever written has a section on this topic, although most of them have different ideas about what it means — e.g., never risk more than 1 to 2 percent of your trading account, take a break after three consecutive losses, stop trading entirely for a period of time if you lose a significant portion of your account, and so on. These are all important concepts

Here's another idea you can implement before you make your first trade: Make sure you have a minimum capitalization of $50,000 when you begin trading, but only deposit 60 percent of it in a trading account. Keep the remainder in a bank from which you can easily transfer it to your trading account as needed. To protect your initial capital, promise yourself that before you lose 40 percent of it, you will quit trading — at least for three to six months — while you get more education, training and experience.

A sound foundation

Just because you have some money does not qualify you to be a professional trader. Spend as much time researching, analyzing and testing trading ideas as you can and you may spend less on trading losses later. Get the best training you can, and then take things slowly and maintain a "wait and see" attitude about whether trading as a career is really for you.

All traders, regardless of how long they have been trading or what prior success they have had, should keep at least $30,000-$50,000 in their accounts at all times.

You must endure to succeed. If you don't plan to invest a sufficient amount of time on developing your skills after obtaining the essential education and training, leave the business now — you'll have a few more dollars in your pocket later.

In these times of frequent layoffs, many people look to trading as a new opportunity.

Consider it as such if you like, but know full well that the learning curve is years — not weeks or even months. If your personal circumstances, financial resources and psychology lend themselves to the isolation and concentration of trading, you're starting off on the right foot.

For information on the author see p. xx.

To take a Trader IQ test based on these principles, go to www.daytradersusa.com/tiqeval.html